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In Conversation With



Fast Growth in E-Commerce Demands New Payments Models

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Fundamentally, banks facilitate industry through the enablement of trade. Are current banking services adequately positioned for today's challenges?

Back to the Future.. Or Back to Normal?

World trade dipped in 2009, due to factors including weak demand, falling commodity prices, the economic crisis and limited access to credit. From there, however, exports have trended back up. The value of global trade rose 13.5% in 2010 to a level similar to the pre-crisis volumes.

So, is everything back to normal then?

The answer is **no**.

The shape of world trade is changing, and rapidly. Economic factors, coupled with mass market adoption of the internet and mobile technology, has massively changed the accessible market opportunity for sellers, and the range of goods buyers can identify and research from their homes. Consequently, e-commerce is growing fast. The number of e-payment transactions in 2010 totaled 17.9 billion, and is expected to grow at a sustained 19.1% a year to total 30.3 billion by 2013.

As traditional banking services are not well suited to e-commerce, and banks are slower to change than the market, there is much more opportunity for payments innovators. Indeed, from almost nowhere, non-bank providers already accounted for about 6.5% of the e-commerce segment in 2010 and are likely to account for nearly 9% or 2.7 billion transactions in 2013. The market is large and growing, with an aggregate value of global e-payments expected to reach €1.4 trillion in 2013.

Meanwhile, back in the real world...

The average value of non-bank e-payments transaction is nearly €45. Banks typically regard a €45 transaction as a 'retail' transaction. Globally around 88% of all cross-border payments are retail transactions. According to Boston Consulting, there were 6.8bn retail cross-border transactions in 2010, compared with 944m wholesale cross-borders.

Within the Eurozone, there are far more retail than wholesale cross-borders. In the second half of 2010, more than 60% of payments in TARGET2 (the European Central Bank RTGS) were for less than €50,000, which it considers to be "retail payments". Many of these payments are processed through wholesale solutions because banks' retail payments systems were designed for a domestic market, and don't easily transform into multicurrency international services.

For banks and payments services providers, new opportunity lies in two dimensions; with smaller stakeholders, and for lower value transactions. More than half of total payments and cash management revenue is generated by small- and midcaps. A survey of corporate payments practitioners recently carried out by Glenbrook Partners confirmed the market gap. Their survey identified challenges and opportunities for smaller businesses, especially those in the \$500 to \$2,000 range.

New markets – but no new solutions?

The research identified how changes in the way cross-border payments are processed could deliver three main benefits: reducing costs (65%), improving payments quality (55%), and improving relationships with suppliers (49%). Glenbrook commented 'We think the opportunities are considerable - one could argue that this is today's largest unsatisfied opportunity in the payments industry.'

Few banks have the capability of delivering such a solution. But the benefits are clear.

A recent survey conducted across 33 European countries found that while just a quarter of European SMEs had undertaken international business relationships or transactions in the last three years, those who did trade internationally were more innovative and grew faster in terms of employment and turnover than those without international reach.

Providing the tools to serve e-commerce is nurturing the profit centres of the future. Equally, the opportunity costs of not doing so are clear, as other countries spread their wings and chase the trade flows. For example, whilst within Europe, the UK, Italy, France and Germany account for nearly 23% of the trade, it is the European emerging markets that are seeing the most significant growth. In the last 10 years, the share of world trade from the Czech Republic has gone up by 111% and in Poland has gone up by 92%.

Time to reflect?

The dilemma is obvious.

The retail-like returns from low value e-commerce payments look unattractive to banks' correspondent banking business. For retail bankers, the investment needed to extend their retail systems internationally is far too great. Consequently, regulated non-bank players in Europe face a substantial and growing opportunity.

Will banks adopt the new models, or continue with the old?

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